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HOUSE OF REPRESENTATIVES

REPORT
99-376

AMENDING THE SMALL BUSINESS INVESTMENT ACT OF 1958

NOVEMBER 14, 1985.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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Mr. MITCHELL, from the Committee on Small Business, submitted the following

REPORT

[To accompany H.R. 3608]

[Including cost estimate of the Congressional Budget Office]

The Committee on Small Business, to whom was referred the bill (H.R. 3608) to amend the Small Business Investment Act of 1958, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

INTRODUCTION AND BACKGROUND

Chairman Mitchell introduced the bill (H.R. 3608) on October 23, 1985. The Subcommittee on SBA and SBIC Authority, Minority Enterprise and General Small Business Problems held a hearing on H.R. 3608 on November 7, 1985. Testifying at the hearing were Edwin T. Holloway, Associate Administrator for Finance and Investment, U.S. Small Business Administration and Peter F. McNeish, Executive Vice President of the National Association of Small Business Investment Companies. The American Association of Minority Small Business Investment Companies submitted a statement for the hearing record.

All witnesses were in support of the legislation, as introduced, and its clarification of Congressional intent for the application of Section 308(i) of the Small Business Act of 1958.

At full Committee markup on November 13, 1985, the Committee by a vote of 38 yeas and no nays ordered the measure favorably reported without amendment.

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NEED FOR THE LEGISLATION

The SBIC industry is regulated in substantial detail by the Small Business Administration. SBA regulations set limits on the terms and conditions of financial transactions between SBIC's and small firms. Section 308(i) of the Small Business Investment Act of 1958 deals with the amount an SBIC is authorized to charge for a loan to a small business.

A Small Business Investment Company is a privately-organized, privately capitalized and privately-managed source of venture capital for new and growing independent businesses. SBIC's are licensed by the Small Business Administration, and comply with broad investment criteria established by law. As an incentive to an SBIC to provide equity capital, long-term loans, and management assistance to small businesses, SBIC's are permitted to borrow funds from the Federal government at an interest rate slightly above the cost of money to the Federal Treasury. The fiscal year 1985 program level for SBIC's was $265 million in guarantees of debentures; in turn, SBIC's made 2,827 investments in small businesses for $438.7 million.

Minority Enterprise Small Business Investment Companies (MESBIC's) are SBIC's which provide the same assistance as SBIC's except they specialize in doing so to small business concerns owned by socially and economically disadvantaged persons. MESBIC's are governed by the same regulations, with some modifications, providing a program that is specially responsive to the needs of the disadvantaged business community. The fiscal year 1985 program level for MESBIC's was $47 million; in turn, they made 1,450 investments in disadvantaged small businesses for $107.2 million.

In 1980 omnibus legislation was enacted to override many State usury laws. Title V of Public Law 96-221 included a provision amending Section 308 of the Small Business Investment Act to override arbitrary and outdated State usury laws which were so low that small concerns were unable to get financing from SBIC's.

It is clear that Congress intended the SBA-established interest rate to govern SBIC loans. The legislative history of Public Law 96-221, the enabling Act for Section 308(i), so states. The Joint Explanatory Statement of the Committee of Conference (House Report 96-842) at page 79 states:

> Separate usury limits administered by the Small Business Administration, will apply to small business investment companies.

After enactment of Public Law 96-221, SBA was able to set SBIC loan ceilings by regulation which started the flow of capital again. Unfortunately, the statute itself has proved confusing and needs to be cleaned up retroactive to its enactment in 1980, thereby ratifying SBA's regulations and clarifying that SBA has the authority to set the maximum cost of money which can be charged by SBIC's. This is similar to the authority which SBA now has over maximum rates charged by lenders on guaranteed loans.

Congress is particularly interest in the SBIC industry because of the present capital shortage which is so hard on small businesses. Small concerns have found traditional sources of financing increas-

ingly inaccessible, and therefore have come to rely heavily on venture capitalists. In return, the venture capitalist usually takes a minority ownership in the company and hopes to be rewarded for his risks with capital gains.

While most SBIC's want an opportunity to share in the growth and potential profits of the small companies they finance, many also will make loans and take debt securities. The interest rate for loans made by an SBIC is subject to an SBA regulatory maximum rate, based on the cost of borrowing from the Federal Financing Bank. As of November 1, 1985, the maximum allowable rate on an SBIC loan is presently 17⅜ percent.

What the Bill Would Do

The legislation, H.R. 3608, amends Section 308(i) of the Small Business Act of 1958, and makes it clear that SBA, by regulation, has the authority to determine the maximum allowable interest rates on loans to small businesses which are made by SBIC's or MESBIC's.

This clarification is made retroactive to the effective date of the establishment of the interest rate limitations: April 1, 1980.

The bill does not affect the rights of states to override the preemption of their usury ceilings as provided in current law.

Conclusion

Small business has proven itself unsurpassed in its ability to create jobs, to innovate, and to foster competition. In recent years, however, Federal policies have inhibited the flow of capital into small companies, contributing to inflation at home and a weakened trade position abroad. This Committee has acted swiftly to provide a technical amendment to end any statutory confusion that would inhibit the flow of SBIC and MESBIC funds to small concerns.

The Federal Government is able to multiply greatly the financial assistance to the small and minority business community by channeling its funds through the SBIC industry rather than directly to small concerns. Small business needs venture capital and the Nation needs the SBIC's proven job creation potential of 65,000 new jobs each year.

Small and minority businesses can play a major role in our economy only if provided with an adequate supply of venture capital. To this end, Congress and the Federal government must encourage investments by SBIC's and MESBIC's which have provided, through fiscal year 1985, $6 billion in financings to more than 78,000 small and minority businesses. Enactment of this legislation will encourage and enable this flow of funds to continue.

Matters Required To Be Discussed Under House Rules

In compliance with clause 2(l)(2) of rule XI of the House of Representatives, the following statement is made relative to the vote on the motion to report H.R. 3608:

> A majority of the Committee voted in person and was actually present and the motion was approved by a recorded vote of 38 ayes and no nays.

In compliance with clause 2(l)(3) of rule XI of the Rules of the House of Representatives, the following statements are made:

With regard to subdivision (A), relating to oversight findings, the Committee finds, in keeping with clause 2(b)(1) of rule X, that this legislation is in full compliance with the provision of this rule of the House which states:

> "In addition, each such committee shall review and study any conditions or circumstances which may indicate the necessity or desirability of enacting new or additional legislation within the jurisdiction of that committee.* * *

With regard to subdivision (B), relating to the statement required by seciton 308(a) of the Congressional Budget Act of 1974, the following statement is made relative to the legislation:

> Section 3(a)(2) of the Congressional Budget Act defines the term "tax expenditures" as those revenue losses attributable to provisions of the Federal tax laws which allow a special exclusion exemption, or deduction, from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability.

None of the provisions of H.R. 3608 deals with taxation and thus, in your Committee's option, this bill does not provide new or increased tax expenditures.

Section 3(a)(2) of the Congressional Budget Act defines the term "budget authority" as authority provided by law to enter into obligations which will result in immediate or future outlays involving Government funds.

Under this definition, it is the final action of Congress that authorizes an agency to enter into obligations which constitutes new budget authority. In those cases which entail: (1) an authorization for an agency to undertake a program; (2) an authorization for appropriation of funds to permit that agency to enter into obligations; and (3) an actual appropriation of such funds, it would be only the final action of Congress in appropriating funds which constitutes the budget authority.

None of the provisions of H.R. 3608 appropriates funds and thus, in your Committee's opinion, the bill does not provide new budget authority. Accordingly, no comparison of budget authority, outlays or tax expenditures or 5-year projections have been made.

With regard to subdivisions (C) and (D), the cost estimate of the Director of the Congressional Budget Office relative to H.R. 3608 follows:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, November 14, 1985.

Hon. PARREN J. MITCHELL,
Chairman, Committee on Small Business, U.S. House of Representatives, Rayburn House Office Building, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has reviewed H.R. 3608, a bill to amend the Small Business Investment Act of 1958, as ordered reported by the House Committee on Small Business, November 13, 1985. We expect that enactment of this leg-

islation would result in no cost to federal, state or local governments.

H.R. 3608 would clarify the provision in the Small Business Investment Act that specifies the maximum interest rates to be charged on loans made by small business investment companies and minority small business investment companies. The bill would result in no change in interest rates and would have no cost to the federal government.

If you wish further details on this estimate, we will be pleased to provide them.

With best wishes,

Sincerely,

JAMES BLUM,
(For Rudolph G. Penner, Director).

No oversight findings or recommendations have been made by the Committee on Government Operations with respect to the subject matter contained in H.R. 3608.

In compliance with clause 2(l)(4), the Committee concludes that the provisions of this legislation in and of themselves will have no inflationary impact on prices and costs in the operation of the national economy.

In compliance with clause 7, rule XIII of the House of Representatives, the Committee makes the following statement:

> The costs attributable to this bill for the current fiscal year and for fiscal years 1987-91 are as follows: This bill amends existing law to make clear that SBA has the authority to set the maximum interest rates on loans made to small businesses by Small Business Investment Companies and Minority Enterprise Small Business Investment Companies. This is merely a housekeeping provision which carries no cost.

No cost estimate was submitted by any Government agency on H.R. 3608 to your Committee.

In your Committee's opinion, the above statements fully comply with the Rules of the House of Representatives.

CHANGES IN EXISING LAW MADE BY BILL, AS REPORTED

In compliance with clause 3 of Rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, H.R. 3608 as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

SECTION 308 OF THE SMALL BUSINESS INVESTMENT ACT OF 1958

SEC. 308. MISCELLANEOUS.—

(a) * * *

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(i)(1) The purpose of this subsection is to facilitate the orderly and necessary flow of long-term loans and equity funds from small business investment companies to small business concerns.

(2) In the case of a business loan, the small business investment company making such loan may charge interest on such loan at a rate which does not exceed [the lowest of the rates described in subparagraphs (A), (B), and (C).

[(A) The rate described in this subparagraph is the maximum rate prescribed by regulation by the Small Business Administration for loans made by any small business investment company (determined without regard to any State rate incorporated by such regulation).

[(B) The rate described in this subparagraph is the maximum rate authorized by an applicable State law or constitutional provision which is not preempted for purposes of this subsection.

[(C)(i) The rate described in this subparagraph is the higher of the Federal Reserve rate or the maximum rate authorized by applicable State law or constitutional provision (determined without regard to the preemption of such State law or constitutional provision).

[(ii) For purposes of clause (i), the term "Federal Reserve rate" means the rate equal to the sum of 1 percentage point plus the discount rate on ninety-day commercial paper in effect at the Federal Reserve bank in the Federal Reserve district in which the principal office of the small business investment company is located.

[(iii) The rate described in this subparagraph shall not apply to loans made in a State if there is no maximum rate authorized by applicable State law or constitutional provision for such loans or there is a maximum rate authorized by an applicable State law or constitutional provision which is not preempted for purposes of this subsection.] *the maximum rate prescribed by regulation by the Administration for loans made by any licensee (determined without regard to any State rate incorporated by such regulation).*

(3) A State law or constitutional provision shall be preempted for purposes of paragraph (2)[(B)] with respect to any loan if such loan is made before the date, on or after April 1, 1980, on which such State adopts a law or certifies that the voters of such State have voted in favor of any provision, constitutional or otherwise, which states explicitly and by its terms that such State does not want the provisions of this subsection to apply with respect to loans made in such State, except that such State law or constitutional or other provision shall be preempted in the case of a loan made, on or after the date on which such law is adopted or such certification is made, pursuant to a commitment to make such loan which was entered into on or after April 1, 1980, and prior to the date on which such law is adopted or such certification is made.

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